Ketua Pengarah Hasil Dalam Negeri & Anor v Maxis Communication Bhd

COURT OF APPEAL (PUTRAJAYA) — CIVIL APPEAL NO W-01–665 OF 2010

SYED AHMAD HELMY, ABDUL WAHAB PATAIL AND ABDUL AZIZ JJCA

20 FEBRUARY 2013

Revenue Law — Income tax — Assessment — Equivalent cash consideration (ECC payment) in lieu of Employee Share Option Scheme — Whether ECC payment was ordinary cash remuneration or share based payment — Whether special provisions on right to acquire shares should apply — Income Tax 1967 ss 25(1A) & 32(1A)

Maxis Communication Bhd ('the respondent') offered its employees an Employee Share Option Scheme ('ESOS Scheme'). When Binariang GSM Sdn Bhd succeeded in its takeover of the respondent, the latter could no longer honour its obligations under the ESOS. The respondent thus proposed an equivalent cash consideration ('ECC'), an alternative consideration that was no longer in the form of shares, in lieu of the ESOS Scheme. The Director-General of Inland Revenue ('the DGIR') was of the opinion that the ECC payment was a salary or ordinary cash remuneration to which s 13(1)(a) of the Income Tax 1967 ('the Act') applied. The respondent argued that s 13(1)(a) of the Act did not apply to the ECC payment. Instead it was the respondent's contention that the ECC payment was a share based payment to which the special provisions on the right to acquire shares under ss 25(1A) and s 32(1A) of the Act would apply. The High Court allowed the respondent's application for judicial review and set aside the DGIR's ruling. This was the DGIR's appeal against that decision.

Held, allowing the appeal with costs fixed at RM15,000:

(1) The ECC exercise, which was not made under the ESOS Scheme per se, was a collateral and separate exercise to relieve the respondent of its ESOS Scheme obligation. Under the ECC exercise, the respondent's employees had no right to specific shares which remained unvested. As the ECC payment was dealing with these unvested shares, the application of the special provisions on the right to acquire shares under ss 25(1A) and 32(1A) of the Act did not arise (see para 11).

(2) The DGIR had not misconstrued the law and there was no reason for judicial intervention by the High Court. The order of the High Court was thus set aside (see paras 1 & 12).

[Bahasa Malaysia summary

Maxis Communication Bhd ('responden') menawarkan kepada pekerja-pekerjanya Skim Opsyen Saham Pekerja ('Skim ESOS'). Apabila Binariang GSM Sdn Bhd berjaya mengambil alih responden, responden tidak lagi dapat menjalankan tanggungjawabnya di bawah ESOS. Responden oleh itu mencadangkan pertimbangan tunai bersamaan ('EEC'), pertimbangan alternatif yang bukan lagi dalam bentuk saham, sebagai ganti Skim ESOS. Ketua Pengarah Hasil Dalam Negeri ('KPHN') berpendapat bahawa pembayaran ECC adalah ganjaran gaji atau wang tunai biasa di mana s 13(1)(a) Akta Cukai Pendapatan 1967 ('Akta') terpakai. Responden berhujah bahawa s 13(1)(a) Akta tidak terpakai kepada pembayaran EEC. Sebaliknya adalah hujahan responden bahawa pembayaran ECC adalah pembayaran berdasarkan saham di mana peruntukan khas atas hak untuk memperoleh saham-saham di bawah ss 25(1A) dan 32(1A) Akta akan terpakai. Mahkamah Tinggi membenarkan permohonan responden untuk semakan kehakiman dan mengetepikan perintah KPHN. Ini adalah rayuan KPHN terhadap keputusan tersebut.

Diputuskan, membenarkan rayuan dengan kos ditetapkan kepada RM15,000:

(1) Pelaksanaan ECC, yang tidak dibuat di bawah Skim ESOS itu sendiri, adalah kolateral dan pelaksanaan berasingan untuk membebaskan responden daripada tanggungjawab Skim ESOSnya. Di bawah pelaksanaan ECC, pekerja-pekerja responden tidak mempunyai hak kepada saham-saham spesifik yang kekal tidak dilaburkan. Memandangkan pembayaran ECC adalah berurusan dengan saham-saham yang tidak dilaburkan ini, permohonan peruntukan khas atas hak untuk memperoleh saham-saham di bawah ss 25(1A) dan 32(1A) Akta tidak berbangkit (lihat perenggan 11).

(2) KPHN tidak salah tafsir undang-undang dan tidak terdapat alasan untuk campur tangan kehakiman oleh Mahkamah Tinggi. Perintah Mahkamah Tinggi oleh itu diketepikan (lihat perenggan 1 & 12).]

Notes

For cases on assessment, see 10 *Mallal's Digest* (4th Ed, 2011 Reissue) paras 2384–2414.

Cases referred to

Palm Oil Research and Development Board Malaysia & Anor v Premium Vegetables Oils Sdn Bhd & another appeal [2005] 3 MLJ 97; [2004] 2 CLJ 265, FC (folld)

Legislation referred to

Income Tax 1967 ss 13, 13(1)(a), 25, 25(1), (1A), 32(1), 32(1A), (a), (b), (c)
Rules of the High Court 1980 O 53 r 2

Appeal from: Judicial Review Application No R3-25–335 of 2008 (High Court, Kuala Lumpur)

Hazlina Hussain (Ahmad Khairuddin Abdullah with her) (Inland Revenue Board of Malaysia) for the appellants.
Rishwant Singh (P Jayasingam and Gandhi Mohan with him) (Zul Rafique & Partners) for the respondent.

Abdul Wahab Patail JCA (delivering judgment of the court):

[1] Having heard the submissions of the parties, this court allowed the appeal with costs fixed at RM15,000. The order of the High Court was set aside and the ruling of the Director-General of Inland Revenue dated 10 October 2008 was affirmed.

[2] The appeal was against the order of the High Court which allowed the respondent's application for judicial review filed under O 53 r 2 of the Rules of the High Court 1980 and setting aside the ruling by the Director-General that:

(a) pursuant to cl 7.1.1 of the ESOS Scheme Byelaws, the options only vested from the date of the first anniversary that the employee is offered the option and not from the date of grant;

(b) consequently, an employee does not have any rights in an unvested option before the date of the first anniversary and the requirement that there be a '… right to acquire shares in a company …' in s 25(1A) of the Act is not fulfilled;

(c) from a legal standpoint, before the amendment to ss 25(1) and 32(1) of the Act, these unamended provisions did not apply to IS because the ECC offered to the employees were not offered in their original form ie as shares and the price has been ascertained without reference to the material market value. It is further not subject to market risks as ordinary ESOS schemes are;

(d) when Maxis employs cl 10.1 of the ESOS Scheme Byelaws, Maxis substitutes the cancellation of the ESOS Scheme with an alternative consideration. In this instance, Maxis' employees are paid an alternative consideration in return for the cancellation of the ESOS Scheme. The alternative consideration is no longer in the form of shares which need to be valued, and to the contrary, it is the receipt of cash arising from employment; and

(e) Maxis' employees are not offered fresh share options as a consequence of the takeover and instead are paid a sum of money the value and timing of which is based on the ESOS Scheme. Further, Maxis' employees do not have to pay anything to receive the said payment and this is different from the ordinary ESOS where an employee has to make payment to enforce the offer of shares given to him.

[3] A brief description of the background is necessary in understanding the issue before the court.

BACKGROUND

[4] There was in place a binding Maxis Employee Share Option Scheme ('ESOS Scheme') offered by Maxis and accepted by its employees. When Binariang GSM Sdn Bhd takeover offer succeeded, Maxis could no longer honour its obligations under the ESOS Scheme. Maxis proposed and the employees accepted in lieu thereof an equivalent cash consideration ('ECC'), the acceptance of which would relieve Maxis of its contractual obligations under the ESOS Scheme to offer shares to participating employees.

[5] The issue is whether:

(a) the ECC payment is ordinary cash remuneration to which s 13(1)(a) of the Income Tax Act 1967 (Revised 1971) applied; or

(b) the ECC payment to release the employee of his right to acquire shares and is gross income to which ss 25(1A) and 32(1A) of the Act applies.

[6] The argument for the respondent is that the ECC payment was to relieve Maxis from having to honour its contractual obligation under the ESOS Scheme and was therefore not a salary or ordinary cash remuneration under s 13(1)(a) of the Act, but was, instead, a share based payment to which the special provisions on the right to acquire shares under ss 25(1A) and 32(1A) of the Act applies.

THE LAW

[7] Gross income of an employee in respect of gains or profits from an employment is defined in s 13 of the Act to include any wages, salary, remuneration, leave pay, fee. Commission, bonus, gratuity, perquisite or allowance (whether in money or otherwise) in respect of having or exercising the employment.

[8] Section 25 concerns the basis period to which the gross income is related. Subsection (1A) provides that the gross income from an employment in respect

of any right to acquire shares in a company of the kind to which para 13(1)(a) applies, shall where the right is exercised, assigned, released or acquired in the relevant period be treated as gross income of the relevant person for that relevant period.

[9] Section 32(1A) sets out the special provisions for determination of the amount to be included in his gross income and the relevant period. It was provided that the amount shall be the market value of the shares:

(a) on the date of; or

(b) on the date specified for; or

(c) the first day of the period specified for the exercise, assignment, release or acquisition of the right to the shares.

[10] Paragraph (b) of sub-s (1A) what is meant by the term market value of the shares.

[11] In our view, s 32(1A) means that the exercise, assignment, release or acquisition of the right to the shares relates to shares an employee is determined to be entitled to since in order for vesting to occur the number of shares awarded or offered must be determined. The ECC exercise does not appear to be part of any such an exercise. Under the ECC, Maxis was in fact to be relieved of the contractual obligation to make such award or offer. There was no vesting of any shares the rights to which may be exercised, assigned, released or acquired. It was not, therefore, made under the ESOS Scheme per se but was a collateral and separate exercise to relieve Maxis of the ESOS Scheme obligation while the shares were not yet awarded or offered and was therefore unvested. Following *Palm Oil Research and Development Board Malaysia & Anor v Premium Vegetables Oils Sdn Bhd & another appeal* [2005] 3 MLJ 97; [2004] 2 CLJ 265 (FC) as to interpretation of a taxing statute, and looking fairly at the language used, it is true there was a binding contractual obligation giving the employees a right to acquire shares under the terms of the scheme, but the actual entitlements remained to be determined, eg the passage of time the employee remained in employment. There was no right to specific shares yet. They remained unvested. The ECC was dealing with these unvested shares. We conclude that the application of ss 25(1A) and 32(1A) does not arise.

[12] It is evident that the High Court has misconstrued the law and the Director-General of Inland Revenue had not. There was no reason for judicial intervention by the High Court.

[13] For the foregoing reasons, we made the decision first above set out.

Appeal allowed with costs fixed at RM15,000.

Reported by Kohila Nesan